STATE OF VERMONT

HUMAN SERVICES BOARD

In re	)	Fair Hearing No. 17,465
	)	
Appeal of	)	

INTRODUCTION

The petitioner appeals a determination by the Department of Prevention, Assistance, Transition, and Health Access (PATH) that he is ineligible for the Vermont Health Access Program (VHAP) because of excess income. The issue is whether the petitioner should be allowed to deduct IRS "Section 179" expenses from his self-employment income.

FINDINGS OF FACT

1. The petitioner is a single person who had been receiving VHAP benefits prior to his most recent review in November of 2001. At that time, the petitioner provided PATH with a copy of his 2000 income tax forms showing what he had earned during the previous year from his self-employment as a real estate appraiser. Following review of that information, PATH notified the petitioner by a letter dated December 3, 2001 that he would no longer be eligible for VHAP after December 31, 2001 based on countable income calculated by the Department to be $1,296.33 per month. This calculation was

based on $1,371.65 monthly earned income from self-employment plus $14.58 per month unearned income from which a $90 standard employment expense amount was deducted.

2. The petitioner’s 2000 Form 1040 showed that he had $4,831 for the year in self-employment income. A profit and loss statement appended to the form showed that the petitioner’s gross income was $77,226. He also itemized expenses of $71,661. One of the expenses itemized was a “Depreciation and Section 179 expense deduction” of $11,630 on line 13. An attached form detailing the “Depreciation and Amortization Expenses” indicated that the petitioner had elected to “expense” $8,706 of the amount on line 13 under "Section 179" of the IRS. A further attachment indicated that the "Section 179" expense represented a partial deduction for several pieces of tangible property purchased for the business during that year including an upgraded computer, office furniture, a digital camera, a FAX machine, and a “4-wheeler”.

3. The Department declined to deduct any of the income from line 13 of the Profit and Loss Statement ($11,360) from its calculations of the petitioner's income. Without this deduction the petitioner's gross income is $1,371.65 per month.

4. The petitioner does not argue that the Department was wrong to exclude the regular “depreciation” amounts on line 13 from his self-employment income but argues that amounts expensed as a "Section 179" deduction should have been deducted from his earnings for the year because they are not strictly speaking “depreciation”. If this method were used, the petitioner would then have a yearly income of $7,755 or a monthly income of $646.25. The Department agrees that this last figure would make him eligible for VHAP benefits.

ORDER

The decision of the Department is affirmed.

REASONS

In order to determine the amount of income countable for eligibility in the VHAP program, regulations adopted by PATH allow the deduction of certain business expenses from gross self-employment income:

Business Expense

> Business expenses, which are deducted from gross receipts to determine adjusted gross income, are limited to operating costs necessary to produce cash receipts, such as:
>
> 1. Office or shop rental; taxes on farm or business property;

2. Hired help;

3. Interest on business loans; and

4. Cost of materials, stock, and inventory, livestock for resale required for the production of this income.

Items such as personal business and entertainment expenses, personal transportation, purchase of capital equipment, depreciation, and payment on the principal of loans for capital assets or durable goods are not allowable business expenses.

Medicaid Manual § 4001.81(d)

The above regulation displays a strong policy against allowing persons to claim income eligibility for state sponsored health care who have spent their income to amass capital assets in a business. This policy is quite different from that of the Internal Revenue Service which encourages the build-up of capital assets in a business by exempting amounts spent in such a way from taxation.

The petitioner's tax consultant has entered into this debate on his behalf arguing that the "Section 179" deduction is really just an ordinary legitimate expense deduction taken for what a business operator paid for an item used in the business in the year it was purchased and is nothing like depreciation which is a deduction that occurs over a number of years according to an asset longevity schedule. He cites in support of his contention the language of 26 USC § 179 saying

that “[a]n expense deduction is provided for taxpayers (other than estates, trust or certain noncorporate lessors) who elect to treat the cost of qualifying property[1] as an expense rather than a capital expenditure”. The Department has countered that "Section 179" is really nothing more than an “accelerated” form of depreciation and points out that this expense method is consistently found in the federal regulations, IRS publications and on tax forms under the rubric of “depreciation”. See, e.g., 26 CFR § 1.1245-2(a)(3)(i), Publication 946 and Form 4562.

In order to decide this case, it is, fortunately, not necessary to untie the Gordian knot of whether "Section 179" deductions should be generally classified as “accelerated depreciation” or simple equipment deductions. This is because PATH’s regulation cited above clearly excludes the purchase of capital assets as well as deductions for depreciation from the definition of business expenses. The parties do not dispute that the furniture, computers, digital cameras and the “four-wheeler” purchased by the petitioner were equipment going into the business. As such, these are not deductible expenses

[1] Qualifying property is defined in IRS Publication 946 as "depreciable property" including tangible personal property (i.e. machines and equipment) purchased for a business.

regardless of whether they are not classified as “depreciation” expenses under the tax code.

PATH was correct to exclude the purchase of these items from profits made by the petitioner when calculating his countable benefits for the VHAP program. As the maximum income for a single individual in the VHAP program is $1,114 per month, the Department is also correct that the petitioner is over the income limit for this program. Procedures Manual 2420B(1). The Board is bound to uphold this decision as it is consistent with the Department's regulations. 3 V.S.A. § 3091(d). Fair Hearing Rule No. 17.

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